January 4, 2008
Japan External Trade Organization（JETRO）

The Expansion of NAFTA-wide Business Operations
~ Summary of the 2007 Survey on the Business Conditions of Japanese Manufacturers in the three NAFTA Countries ~

The North American Free Trade Agreement (NAFTA), which came into effect in January 1994, celebrates its 15th anniversary in 2008. The process of tariff liberalization, which has been gradually put into practice, will be completed in 2008. On the other hand, with the recent rise of emerging countries such as China and the ASEAN nations, NAFTA's trade relationships with these countries and regions have strengthened. As a result, since it hit a peak of 48.8% in 2000, NAFTA's intra-regional trade ratio has been declining (44.2% in 2006). The decline of the intra-regional import ratio has been especially significant since it peaked at 41.1% in 1999 (34.3% in 2006). Under these circumstances, the Japan External Trade Organization (JETRO) conducted a survey on the business conditions of Japanese manufacturers operating in the NAFTA countries, including their utilization of the free trade agreement. There are several free trade agreements (FTAs), either concluded or still under negotiation, between Asian and NAFTA countries. Among these are the Japan-Mexico Economic Partnership Agreement (EPA), which came into effect in 2005, the yet-to-be-ratified US-Korea FTA, and the Canada-Korea FTA, which is under negotiation.

The 2007 survey sent out questionnaires to Japanese manufacturers operating in the NAFTA countries inquiring about:
1) their utilization of NAFTA,
2) the impact of other EPAs and FTAs on their business locations and
3)the relocation of their business operations or construction of new facilities within/outside the NAFTA countries.

The results of the survey show that:
1) the expansion of NAFTA-wide business operations continues especially in the area of transportation equipment components,
2) the Japanese manufactures based in Mexico are largely receiving benefits from the Japan-Mexico EPA, and
3) with regard to a Japan-US FTA proposed by the business community, there is strong interest in the elimination of tariffs and the simplification of the US visa process.

A total of 778 Japanese manufactures replied to the questionnaire, 618 of which are operating in the US, 105 in Canada, and 55 in Mexico. The survey was conducted from July to August in 2007.

1. High utilization of NAFTA

With regard to NAFTA's preferential tariffs, while approximately 40% of the Japanese manufacturers based in the US answered that they receive preferential tariffs "on almost all items" or "on some items", the number reached 60% and a little short of 90% among those based in Canada and Mexico, respectively (Figure 1). Compared to the utilization of the preferential tariff system of the host countries by Asia-based Japanese manufacturers, the rate among the NAFTA countries was relatively high (among those based in Asia, it was 16.7% for exports and 19.2% for imports, according to JETRO's survey conducted between November and December 2006). In the US, this rate was high among the transportation equipment (76.9%), rubber products (71.4%), and transportation equipment components (52.5%) industries. In Canada, it was highest in the transportation equipment components (86.7%) and electrical and electronic components (83.3%) industries; and in Mexico, it was highest in the electrical machinery and electronic devices (100%), transportation equipment components (91.7%), and electrical and electronic components (88.9%) industries. This shows that Japanese manufacturers based in Canada and Mexico are utilizing NAFTA primarily for export purposes. The area common to the three countries is that of transportation equipment components, which provides evidence to support the deepening intra-regional division of labor in the automotive industry.

2. Japan-Mexico EPA: many manufacturers enjoy the benefit

With regard to the Japan-Mexico EPA, more than 50% of the Japanese companies based in Mexico, especially manufacturers of transportation equipment and transportation equipment components, said there are advantages to the EPA (52.8%) (Figure 2). As for the area where the Japan-Mexico EPA had the most profound effect, tariff elimination was ranked number one (87.2%) (Figure 3).

3. US-Korea FTA and Canada-Korea FTA: 70% say they are not affected

With regard to the US-Korea FTA which still awaits congressional ratification, approximately 70% of the US-based Japanese manufacturers (70.7%) said that it would not affect them (Figure 4). On the other hand, more than 20% (23.0%) said there would be more negative effects. Transportation equipment (45.5%), metal products (36.6%), and general machinery (34.9%) were among their areas of concern. Among the Mexico-based Japanese companies, which are closely related to the US market, almost 70% of the respondents (65.5%) said they would not be affected by the US-Korea FTA (Figure 5). However, 30% of them said the US-Korea FTA would affect them, and the percentage was especially high among the electrical machinery and electronic devices (66.7%), and the electrical and electronic components (55.6%) industries. With regard

to the Canada-Korea FTA, for which negotiations are still underway, about 70% of the Canada-based Japanese companies (67.1%) said the free trade agreement would not affect them (Figure 6).

4. The US-led NAFTA-wide business expansion continues ~ as intra-regional relocation to Mexico etc. goes on, new factories are being constructed.

US-based Japanese manufacturers have also been active in relocating their operations. Regarding capital investment, comparing the investment of the past 1-2 years with that of the next 1-2 years, the number of companies constructing new facilities slightly increases (Figure 7, 8). Regarding relocation outside the country, more companies are relocating to Mexico than to China, both in the past and in the next 1-2 years (Figure 9, 10). This shows their business operations are expanding NAFTA-wide. The relocation of production to Mexico is noteworthy in the transportation equipment components industry. This shows that NAFTA's intra-regional division of labor in the automotive industry is intensifying in Mexico, an effect of the Japan-Mexico EPA.

On the other hand, while the construction of new factories in the Southern part of the US and Canada was more visible over the past 1-2 years, (Figure 11), more companies are expected to consider the construction of new facilities in Mexico in the next 1-2 years (Figure 12).

5. Strong interest in tariff elimination and simplification of visa procedures under a Japan-US FTA.

In October 2007, the Nippon Keidanren (Japan Business Federation) proposed the establishment of a Japan-US EPA in its policy proposal titled "A call for the development and promotion of proactive external economic strategies". Under such circumstances, the survey results showed that these companies raised tariff elimination (65.4%) and the simplification of the US visa process (54.5%) as the two biggest advantages a Japan-US FTA could bring to their businesses (Figure 13). There are more voices calling for the establishment of a Japan-US FTA, since Japanese companies fear that they would suffer a relative disadvantage once the US-Korea FTA comes into effect. They are also concerned that US border/customs control policies, which have been tightened since the 9/11 terrorist attacks, would have a negative impact on their business operations.

One fourth of US-based Japanese companies (24.8%) answered that they would increase their utilization of NAFTA, should a Japan-US FTA be established (Figure 14). This rate is high among nontraditional industries such as wood and paper products (33.3%), pharmaceutical products (33.3%), as well as transportation equipment (37.5%), general machinery (32.4%), and metal products (31.8%). Based on these

findings, it is expected that NAFTA-wide business operations will expand much further in the coming years.

Source: 2007 Survey on the Business Conditions of Japanese manufacturers in the three NAFTA countries, and its figures.

Figure 1: The current utilization of NAFTA's preferential tariffs (all countries)
(US: N=568, Canada: N=88, Mexico: N=55)

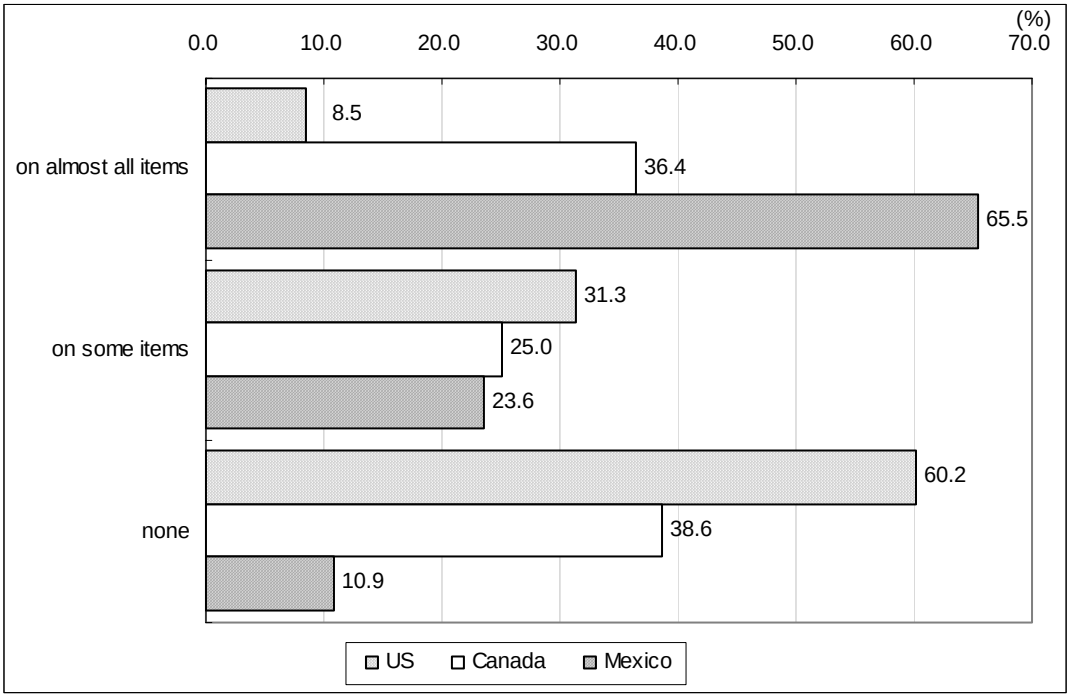


Figure 2: Advantages of the Japan-Mexico EPA (Mexico: N=53)

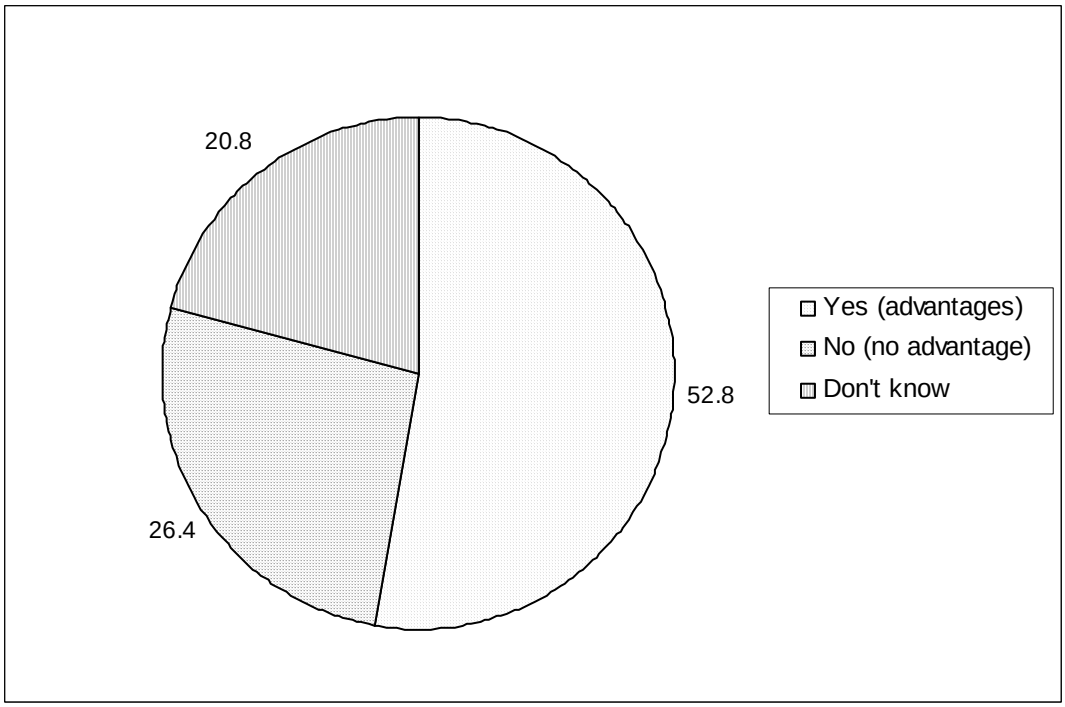


Figure 3: Items with the largest expected impact of the Japan-Mexico EPA
(check all that apply) (Mexico: N=47)

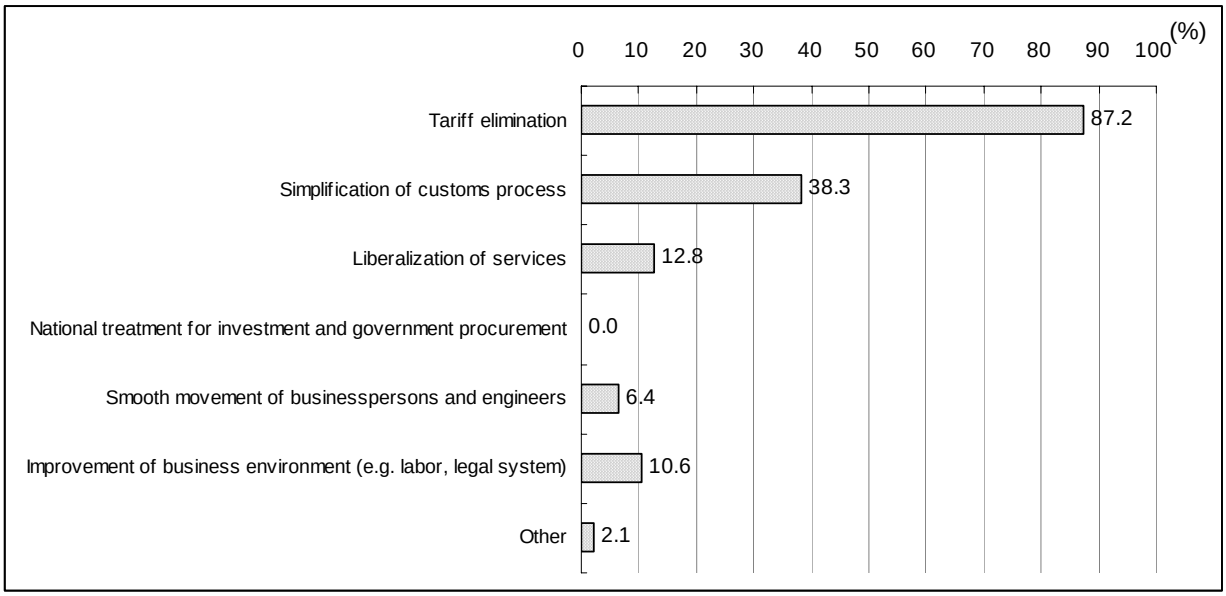


Figure 4: Impact of the US-Korea FTA (US: N=566)

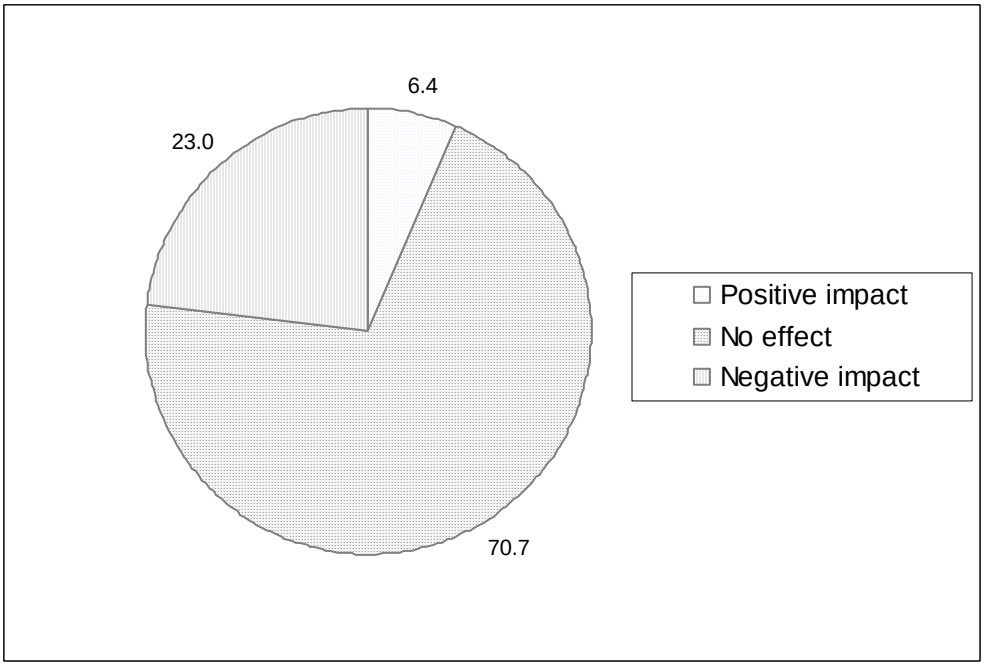


Figure 5: Impact of the US-Korea FTA (Mexico: N=55)

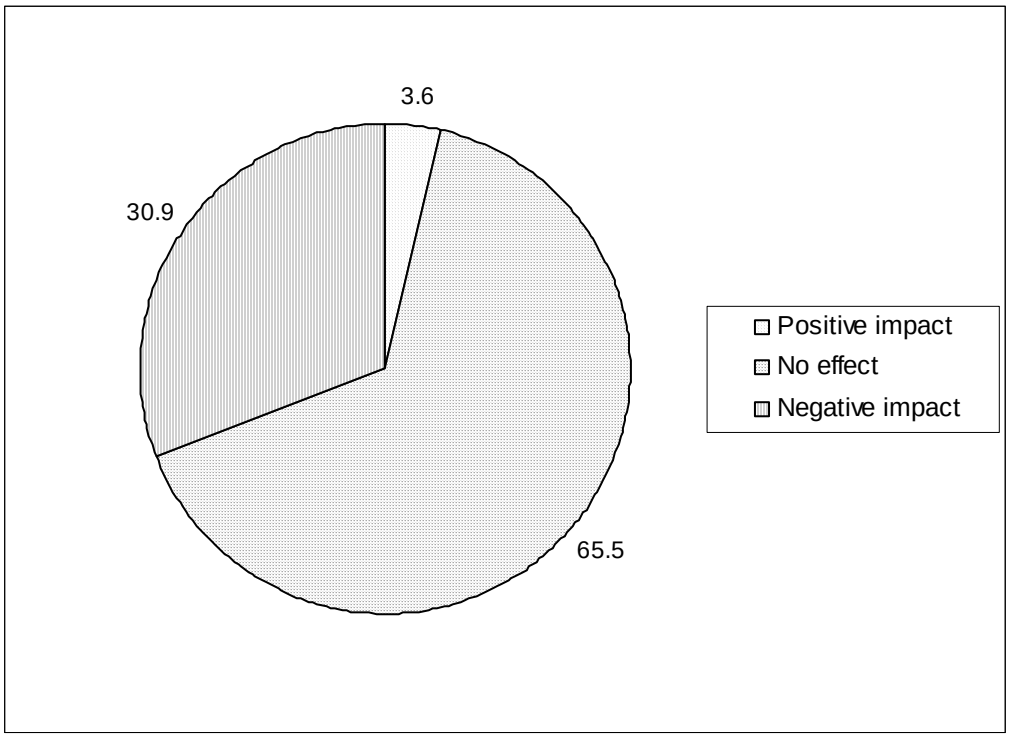


Figure 6: Impact of the Canada-Korea FTA (Canada: N=85)

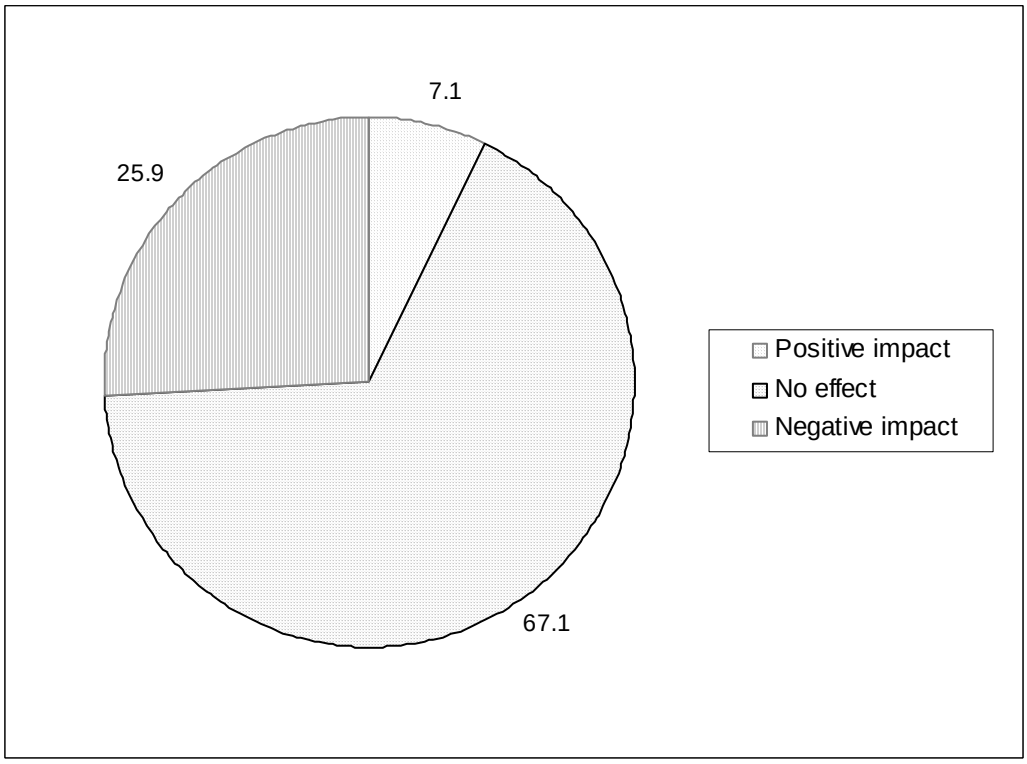


Figure 7: Withdrawals/Factory Closures, relocation of production (past 1-2 years)
(US: N=617)

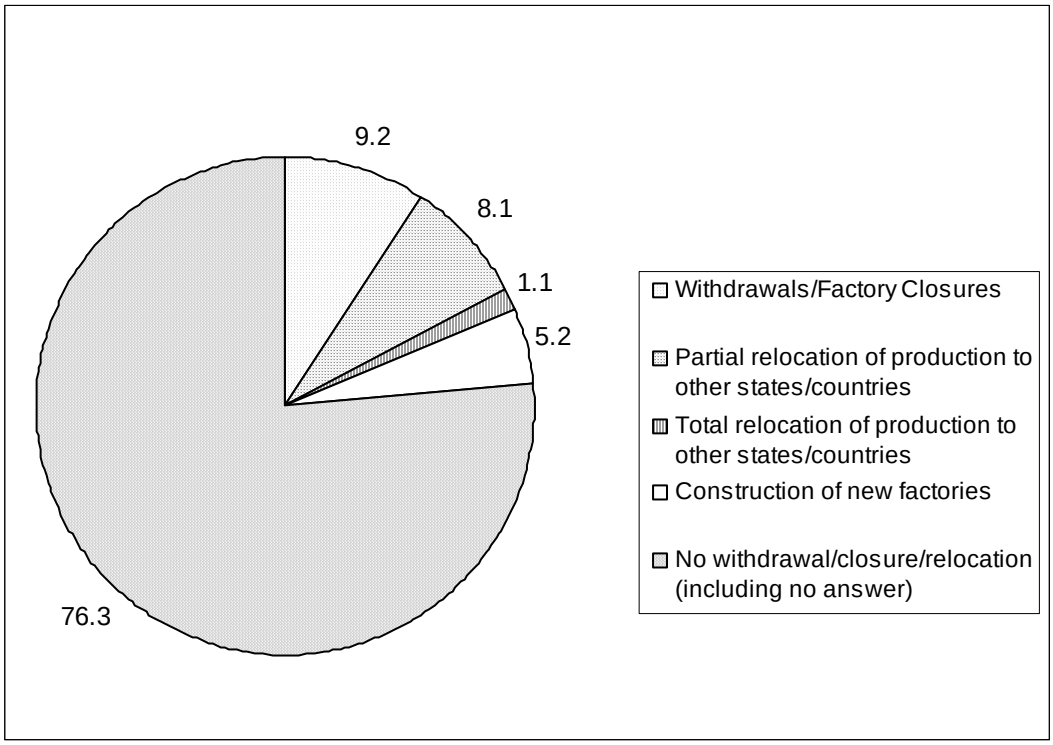


Figure 8: Withdrawals/Factory Closures, relocation of production (next 1-2 years)
(US: N=617)

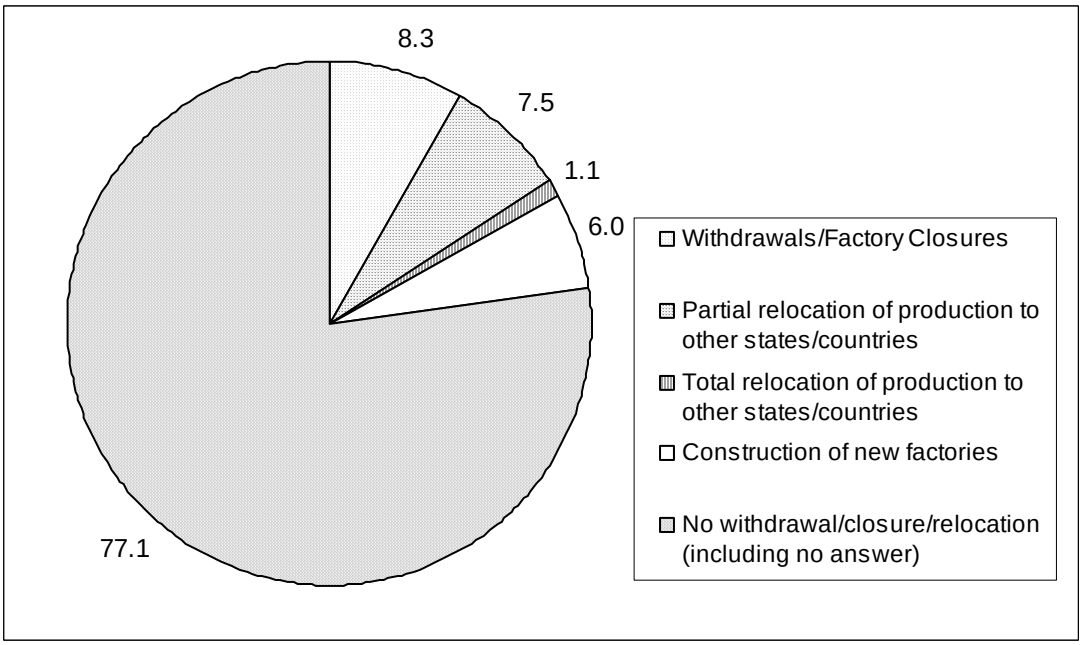


Figure 9: Destinations for relocation
Partial relocation of production to other states/countries (past 1-2 years) (US)

Rank	Countries/US states	Number of companies
1	Mexico	10
	Transportation equipment components (automobile/two-wheeled motor vehicle)	7
	Electrical machinery and electronic devices	2
	Plastic products	1
2	China	9
	Electrical and electronic components	4
	Chemical goods	2
	Transportation equipment components (automobile/two-wheeled motor vehicle)	2
	Clothing/Textiles	1
3	Japan	4
	Rubber products	1
	Paper/Pulp	1
	Electrical and electronic components	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
4	Tennessee	2
	Transportation equipment components (automobile/two-wheeled motor vehicle)	2
	Chemical goods	1
5	Illinois	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
5	North Carolina	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
5	Virginia	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
5	Mississippi	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
5	Canada	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
5	France	1
	Chemical goods	1
5	Turkey	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
5	Asia	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
5	Philippines	1
	Non-ferrous metals	1
5	Vietnam	1
	Other	1
5	Malaysia	1
	Other	1

Figure 10: Destinations for relocation

Partial relocation of production to other states/countries (next 1-2 years)(US)

Rank	Countries/US states	Number of companies
1	Mexico	10
	Transportation equipment components (automobile/two-wheeled motor vehicle)	9
	Plastic products	1
2	China	7
	Transportation equipment components (automobile/two-wheeled motor vehicle)	2
	Plastic products	1
	Clothing/Textiles	1
	Furniture/Home furnishings	1
	Precision machinery	1
	Other	2
3	Japan	5
	Paper/Pulp	1
	Precision machinery	1
	Lumber/Wood products	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
	Other	1
4	Canada	4
	Plastic products	1
	Sales companies	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
	Others	1
5	Illinois	2
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
	Chemical goods	1
5	US domestic-others	2
	Transportation equipment components (automobile/two-wheeled motor vehicle)	2
7	Indiana	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	Ohio	1
	Rubber products	1
7	Kentucky	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	Georgia	1
	Food/Agricultural processing	1
7	Texas	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	Tennessee	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	North Carolinia	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	Virginia	1
	Food/Agricultural processing	1
7	Michigan	1
	Plastic products	1
7	Mississippi	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	Louisiana	1
	Rubber products	1
7	Thailand	1
	Other	1
7	Malaysia	1
	Chemical goods	1
7	Vietnam	1
	Other	1
7	Brazil	1
	Chemical goods	1

Figure 11: Destinations for relocation
Construction of new factories (past 1-2 years)(US: N=456)

Rank	Countries/US states	Number of companies
1	Texas	6
	Transportation equipment (automobile/two-wheeled motor vehicle)	3
	Transportation equipment components (automobile/two-wheeled motor vehicle)	2
	Other	1
2	Canada	3
	Food/Agricultural processing	1
	Steel (including cast and wrought products)	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
3	California	3
	General machinery (including gold molds and mechanical tools)	1
	Chemical goods	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
4	Tennessee	2
	Transportation equipment components (automobile/two-wheeled motor vehicle)	2
4	Alabama	2
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
	Petroleum products	1
4	Georgia	2
	General machinery (including gold molds and mechanical tools)	1
	Metal products (including plated metals)	1
7	Arkansas	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	Alaska	1
	Non-ferrous metal	1
7	Virginia	1
	Chemical goods	1
7	Mississippi	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	Louisiana	1
	Chemical goods	1
7	Vietnam	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	Mexico	1
	Plastic products	1

Figure 12: Destinations for relocation
Construction of new factories (next 1-2 years)(US)

Rank	Countries/US states	Number of companies
1	Mexico	4
	Transportation equipment components (automobile/two-wheeled motor vehicle)	2
	Chemical goods	1
	Ceramic/Soil and Stone	1
2	Mississippi	3
	Transportation equipment (automobile/two-wheeled motor vehicle)	2
	Other	1
3	Illinois	2
	Steel (including cast and wrought products)	1
	Metal products (including plated metals)	1
3	Texas	2
	General machinery (including gold molds and mechanical tools)	1
	Chemical goods	1
3	Indiana	2
	Transportation equipment components (automobile/two-wheeled motor vehicle)	2
3	Canada	2
	Transportation equipment components (automobile/two-wheeled motor vehicle)	2
7	Arkansas	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	Iowa	1
	Chemical goods	1
7	Alabama	1
	Steel (including cast and wrought products)	1
7	Arizona	1
	Plastic products	1
7	Wisconsin	1
	General machinery (including gold molds and mechanical tools)	1
7	Kentucky	1
	Metal products (including plated metals)	1
7	Georgia	1
	Non-ferrous metal	1
7	North Carolina	1
	Other	1
7	Florida	1
	Rubber products	1
7	Massachusetts	1
	Precision machinery	1
7	Michigan	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	Louisiana	1
	Chemical goods	1
7	Southern US	1
	Other	1
7	India	1
	Transportation equipment components (automobile/two-wheeled motor vehicle)	1
7	China	1
	Food/Agricultural processing	1
7	South America	1
	Chemical goods	1

Figure 13: Advantages expected upon establishment of a Japan-US FTA
(check all that apply)(US: N=558)

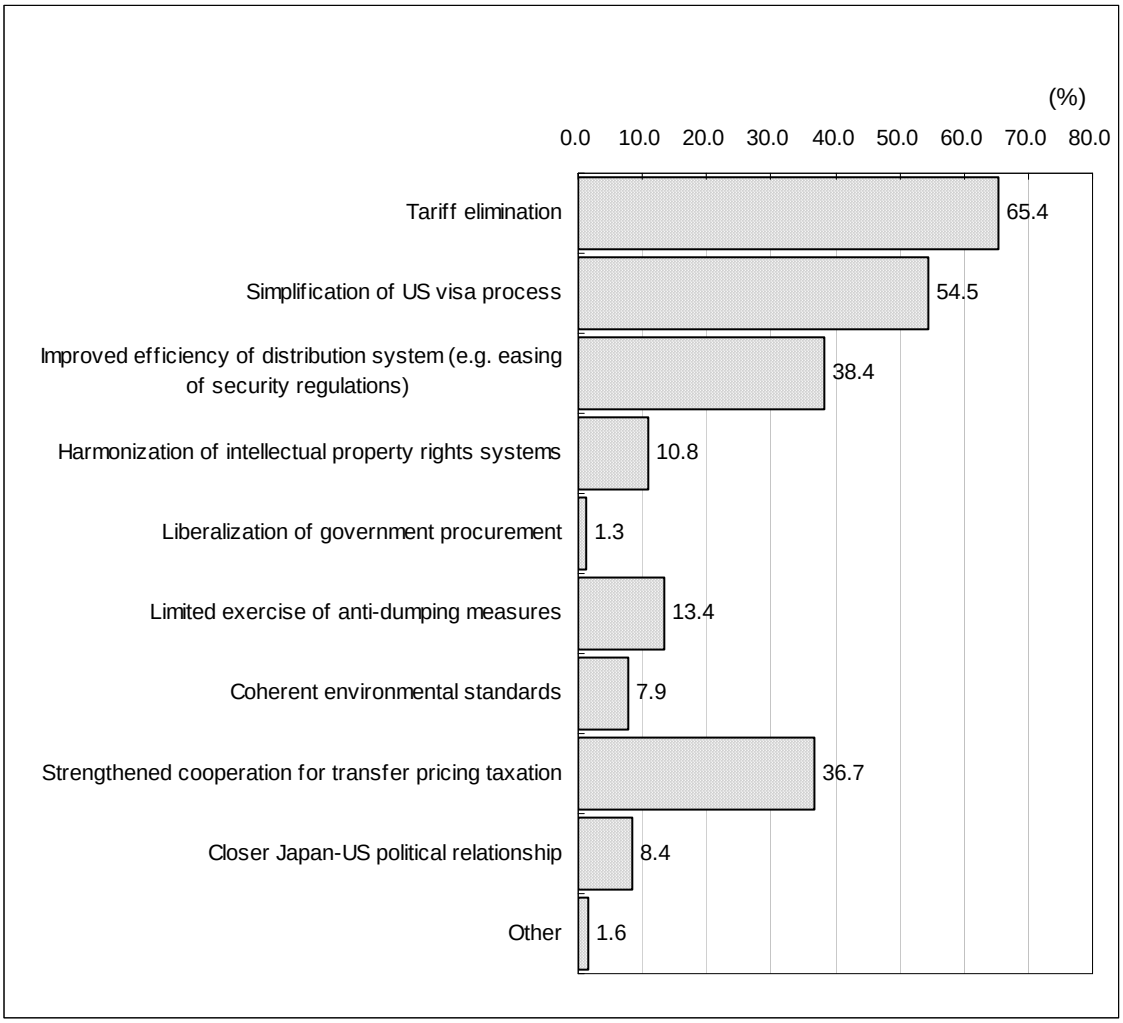
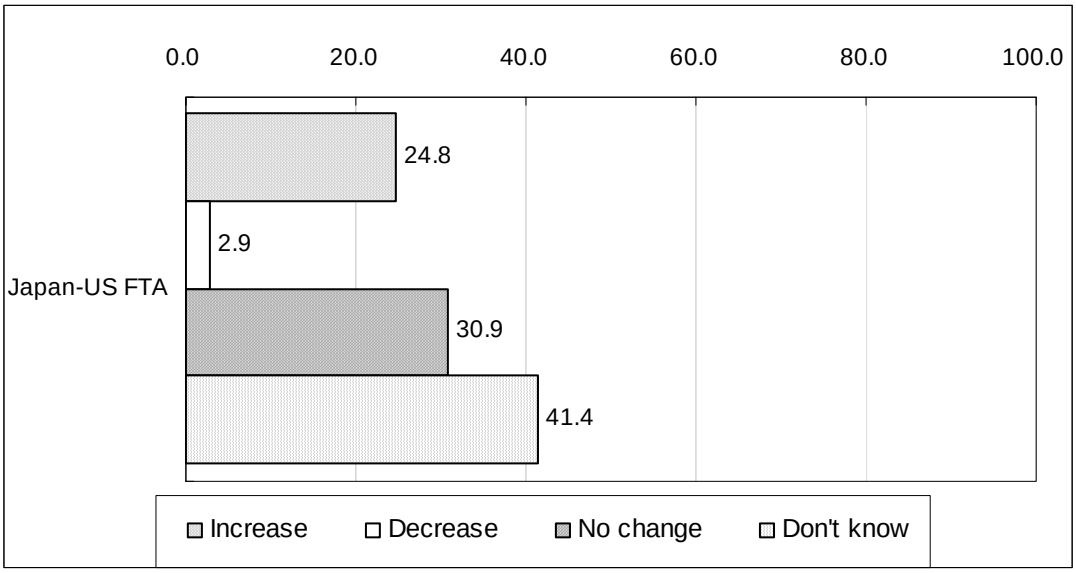


Figure 14: Expected changes in the level of utilization of NAFTA upon realization of a Japan-US FTA (US: N=456)



C.F. The transition of the NAFTA's intra-regional trade ratio (percentage: %)

	1995	1998	1999	2000	2001	2002	2003	2004	2005	2006
NAFTA intra-regional import rate	38.4	41.0	41.1	40.5	40.1	38.7	37.3	35.8	35.3	34.3
NAFTA intra-regional export rate	46.2	51.7	54.6	55.7	55.5	56.6	56.1	55.9	55.1	53.8

Source: "International Financial Statistics", IMF